

# Report of the auditor-general to Eastern Cape Provincial Legislature and the Council of Mquma Local Municipality

## Report on the audit of the financial statements

### Adverse opinion

1. I have audited the financial statements of the Mquma Local Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2018, the statement of financial performance, statement of changes in net assets, cash flow statement and statement of comparison of budget information with actual information for the year then ended, as well as the notes to the financial statements, including a summary of significant accounting policies.
2. In my opinion, because of the significance of the matters described in the basis for adverse opinion section of my report, the financial statements do not present fairly, in all material respects, the financial position of the Mquma Local Municipality as at 30 June 2018, and its financial performance and cash flows for the year then ended in accordance with South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act, 2017 (Act No. 3 of 2017) (Dora).

### Basis for adverse

#### Property, plant and equipment

3. The municipality did not recognise property, plant and equipment (PPE) in accordance with GRAP 17, *Property, plant and equipment*. This was due to the following:
  - Amounts were capitalised to PPE which did not meet the definition of PPE;
  - Items of PPE were included more than once in the asset register;
  - The PPE register incorrectly includes items that should be classified as investment property;
  - Depreciation was calculated incorrectly;
  - Residual values and useful lives of fully depreciated PPE were not reassessed.
4. As a result, PPE is overstated by R1,1 billion (2017: R1,07 billion); accumulated surplus is overstated by R1,04 billion (2017: R1,04 billion); depreciation expense is understated by R27,0 million (2017: R27,0 million); and investment property is understated by R1,7 million (2017: R1,7 million).
5. I was unable to obtain sufficient appropriate audit evidence that PPE for the current and prior years had been properly accounted for, because management did not perform an assessment of the indicators of impairment for PPE as required by GRAP 21, *Impairment of non-cash generating assets*. My audit procedures identified indicators of impairment that should have been

assessed by management. I was unable to confirm the PPE balance by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to the PPE disclosed as R1,6 billion (2017: R1,6 billion) in the statement of financial position and note 8 to the financial statements.

### Investment property

6. The municipality did not recognise investment property in terms of GRAP 16, *Investment Property*. This was due to the following:
- Investment property was recognised more than once in the register
  - PPE was incorrectly recognised as investment property
  - Depreciation was not provided for on some investment properties.
7. As result, investment property disclosed in the statement of financial position and note 7 was overstated by R67,6 million (2017: R67,1 million); PPE disclosed in the statement of financial position and note 8 is understated by R16,3 million (2017: R16,3 million); accumulated surplus disclosed in the statement of financial position and statement of changes in net assets is understated by R50,2 million (2017: R50,2 million); and the depreciation expense disclosed in the statement of financial performance and note 28 is understated by R0,560 million (2017: R0,560 million).

### Receivables from non-exchange transactions

8. I was unable to obtain sufficient appropriate audit evidence that management had properly accounted for receivables for traffic fines in accordance with GRAP 104, *Financial instruments*. GRAP 104, *Financial instruments* requires an entity to disclose an analysis of financial assets that are individually determined to be impaired as at the end of the reporting period, including the factors the entity considered in determining that they are impaired at the end of each reporting period. I was unable to determine whether any adjustments were necessary to receivables from non-exchange transactions stated at R5,1 million (2017: R7,9 million) in the statement of financial position and note 4 to the financial statements. Additionally, there was a resultant impact on the debt impairment for the period, as disclosed in the statement of financial performance and note 30 to the financial statements.

### Receivables from exchange transactions

9. GRAP 104, *Financial instruments* requires an entity to assess at the end of each reporting period whether there is any objective evidence that a financial asset or group of financial assets is impaired. The municipality impaired some of its receivables from exchange transactions that were not supposed to be impaired and incorrectly recognised some properties as billed more than once. As a result, receivables from exchange transactions are understated by R5,3 million (2017: R3,6 million); revenue from non-exchange is overstated by R0,934 million (2017: R1,8 million); and debt impairment is overstated by R6,3 million (2017: R5,4 million). Additionally, there was a resultant impact on the debt impairment for the period as disclosed in the statement of financial performance and note 30 to the financial statements.

## Inventories

10. I was unable to obtain sufficient appropriate audit evidence that management had properly accounted for land inventories in accordance with GRAP 12, *Inventories*. This was due to non-submission of information to support the values of inventory recorded in the accounting records. I was unable to confirm the inventory balance by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to inventories stated at R4,8 million (2017: R5,6 million) in the statement of financial position and note 2 to the financial statements.

## Vat receivable

11. I was unable to obtain sufficient appropriate audit evidence that management had properly accounted for the Vat receivable in the statement of financial position due to the status of the accounting records. I was unable to confirm the Vat receivable balance by alternative means. Consequently, I was unable to determine whether any adjustments were necessary to the Vat receivable stated at R13,9 million (2017: R6,9 million) in the statement of financial position and note 5 to the financial statements.

## Payables from exchange transactions

12. The municipality did not record all its payables from exchange transactions in accordance with GRAP 1, *Presentation of financial statements*. As a result, payables from exchange transactions are overstated by R3,4 million; leave accrual expense is overstated by R1,3 million; PPE is overstated by R1,3 million; general expenditure is overstated by R0,757 million; and agency fees expenditure is overstated by R0,362 million.
13. I was unable to obtain sufficient appropriate audit evidence that payables from exchange transactions had been properly accounted for due to the status of the accounting records. I was unable to confirm the payables from exchange transactions by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to the payables from exchange transactions of R67,8 million (2017: R61,2 million) disclosed in the statement of financial position and note 10 to the financial statements.

## General expenditure

14. The municipality did not recognise expenditure in accordance with GRAP 1, *Presentation of financial statements*. This was due to the following:
- Prior year expenditure was recorded in the current financial year
  - Current year expenditure was not recorded in the financial statements
  - Invoices were processed at the incorrect amounts.
15. As a result, general expenditure disclosed in the statement of financial performance was overstated by R3,8 million and payables from exchange transactions disclosed in the statement of financial position were overstated by R3,8 million.
16. In the previous year, I was unable to obtain sufficient appropriate audit evidence that general expenditure disclosed in the 2016-17 financial statements, which form the basis for the corresponding figures disclosed in the 2017-18 financial statements, had been properly accounted for. This was due to lack of supporting information and records. The required

information was also not submitted in the current financial year. As a result, I was unable to confirm the corresponding figures for expenditure by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to the corresponding figures for collection costs, repairs and maintenance, bulk purchases, grants and subsidies expenditure and general expenses totalling R111,1 million as disclosed in the statement of financial performance.

### Commitments

17. GRAP 17, *Property, plant and equipment* requires the entity to disclose contractual commitments for acquisition of PPE. The municipality did not fully comply with this requirement as the commitments register included contracts that had expired and some contract expenditure was recorded in the register at incorrect amounts. As a result, commitments disclosed in note 37 were overstated by R60,8 million (2017: R74,3 million).

### Irregular expenditure

18. The municipality did not identify and disclose all irregular expenditure in the notes to the financial statements, as required by section 125(2)(d) of the MFMA. Payments made in contravention of the supply chain management (SCM) requirements resulted in irregular expenditure of R48,2 million (2017: R10,6 million) being identified during the audit that was not disclosed. I was unable to determine the full extent of the irregular expenditure that should have been disclosed. Accordingly, I could not determine the adjustment required to the irregular expenditure disclosed at R461,2 million (2017: R424 million) in note 44 to the financial statements.
19. The corresponding figure of irregular expenditure disclosed in note 44 includes an amount of R4,8 million for which there are no supporting documents. Even after considering alternative procedures, I could not obtain sufficient appropriate evidence that the transactions making up this amount were irregular. Consequently, I could not determine whether any adjustments were required to the corresponding figure and the current year closing balance of irregular expenditure disclosed in note 44.

### Prior period error

20. The disclosure of prior period errors in note 48 to the financial statements did not comply with the requirements of GRAP 3, *Accounting policies, estimates and errors*. The nature and the amount of the correction for each financial statement item affected and the amount of the correction at the beginning of the earliest previous period were not disclosed.
21. In addition, I was unable to obtain sufficient appropriate audit evidence for restatements totalling R11,7 million as the supporting information could not be provided. I was unable to obtain the required evidence by applying alternative procedures. As a result, I was unable to determine whether any further adjustments were required to the prior period errors as disclosed in note 48 to the financial statements.

### Statement of comparison of budget and actual amounts

22. The municipality did not disclose the statement of comparison of budget and actual amounts for the cash flow statement in the financial statements, as required by GRAP 24, *Presentation of budget information in the financial statements*. In addition, there were no explanations for some material differences between the budgeted and actual figures as disclosed in the statement of comparison versus actual amounts.



## Cash flow statement

23. The municipality incorrectly classified and incorrectly calculated various line items in the cash flow statement. This resulted in the following line items being misstated as described:

- Sale of goods and services is overstated (2017: understated) by R0,928 million (2017: R4,3 million)
- Employee costs are overstated by R3,1 million
- Suppliers are understated by R1,3 million (2017: R6,1 million)
- The corresponding figure of proceeds from sale of property, plant and equipment is overstated by R1,1 million.

## Corresponding figures

### Revenue from non-exchange transactions

24. In the previous year, I was unable to obtain sufficient appropriate audit evidence that revenue from non-exchange transactions had been properly accounted for due to the status of the accounting records, and supporting documentation used for revenue recognition was not availed for audit purposes. During the current year I was again not provided with the evidence required to substantiate these transactions. I was unable to confirm the revenue from non-exchange transactions by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to the corresponding figure of revenue from non-exchange transactions stated at R308,8 million in the statement of financial performance.

## Context for the opinion

25. I conducted my audit in accordance with the International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the auditor-general's responsibilities for the audit of the financial statements section of this auditor's report.
26. I am independent of the municipality in accordance with the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* (IESBA code) and the ethical requirements that are relevant to my audit in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.
27. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my adverse opinion.

## Material uncertainty relating to going concern

28. I draw attention to the matter below. My opinion is not modified in respect of this matter.
29. I draw attention to note 40 to the financial statements which indicates that the municipality is experiencing financial difficulties in that its current liabilities exceed its current assets. The events or conditions disclosed in note 40, together with other matters set forth in the same note, indicate that material uncertainty exists that may cast significant doubt on the municipality's ability to continue funding its existing level of operations.

## **Emphasis of matters**

30. I draw attention to the matters below. My opinion is not modified in respect of these matters.

### **Unauthorised expenditure**

31. As disclosed in note 42 to the financial statements, unauthorised expenditure to the amount of R276,39 million (2017: R245,12 million) has accumulated over a number of years and has not been condoned.

### **Fruitless and wasteful expenditure**

32. As disclosed in note 43 to the financial statements, fruitless and wasteful expenditure to the amount of R4,17 million (2017: R3,83 million) has accumulated over a number of years and has not been condoned.

## **Other matter**

33. I draw attention to the matter below. My opinion is not modified in respect of this matter.

### **Unaudited disclosure notes**

34. In terms of section 125(2)(e) of the MFMA, the municipality is required to disclose particulars of non-compliance with the MFMA in the financial statements. This disclosure requirement did not form part of the audit of the financial statements and accordingly I do not express an opinion thereon.

### **Responsibilities of the accounting officer for the financial statements**

35. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with SA Standards of GRAP and the requirements of the MFMA and Dora, and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

36. In preparing the financial statements, the accounting officer is responsible for assessing the Mngquma Local Municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the appropriate governance structure either intends to liquidate the municipality or to cease operations, or has no realistic alternative but to do so.

## **Auditor-general's responsibilities for the audit of the financial statements**

37. My objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with the ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

38. A further description of my responsibilities for the audit of the financial statements is included in the annexure to this auditor's report.

## Report on the audit of the annual performance report

### Introduction and scope

39. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report material findings on the reported performance information against predetermined objectives for selected objectives presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.
40. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated the completeness and appropriateness of the performance indicators/ measures included in the planning documents. My procedures also did not extend to any disclosures or assertions relating to planned performance strategies and information in respect of future periods that may be included as part of the reported performance information. Accordingly, my findings do not extend to these matters.
41. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the following selected objectives presented in the annual performance report of the municipality for the year ended 30 June 2018:

Key performance areas	Pages in the annual performance report
KPA 2: Basic services and infrastructure development	x – x
KPA 3: Local economic development	x – x

42. I performed procedures to determine whether the reported performance information was properly presented and whether performance was consistent with the approved performance planning documents. I performed further procedures to determine whether the indicators and related targets were measurable and relevant, and assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete. The material findings in respect of the usefulness and reliability of the selected programmes are as follows:

## KPA 2: Basic services and infrastructure development

### Reliability

#### Reported achievement not supported by sufficient appropriate audit evidence

##### 6 956 beneficiaries subsidised with free basic electricity by June 2018

43. I was unable to obtain sufficient appropriate audit evidence for the reported achievement of 6 956 beneficiaries subsidised with free basic electricity that was reported against the above-mentioned target and indicator. This was due to limitations placed on the scope of my work. I was unable to confirm the reported achievement by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievement of 6 956 beneficiaries subsidised with free basic electricity by June 2018, as disclosed in the annual performance report.

### Usefulness

#### Various indicators

##### Measures taken to improve performance not corroborated

44. I was unable to obtain sufficient appropriate audit evidence to support the measures taken to improve performance against target as reported in the annual performance report. This was due to limitations placed on the scope of my work. I was unable to confirm the reported measures taken by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported measures taken to improve performance for the indicators listed below:

Indicator description	Planned target	Actual Performance
<b>Roads construction:</b> 50 kms of municipal access roads (Dyam-Dyam AR – 7 km, Gubevu to Sawutana AR- 4,6 km, Ngxalathi AR -2 km, Ncerana AR – 2,8 km, Blue Sky AR – 5 km, Ngqwarha to Manyube AR – 3 km, Macibe AR – 7,6 km, Mpahleni AR – 7,1 km, Lusuthu to Masele AR - 3,9 km and Litchi to Qolweni AR – 7 km) constructed by June 2018	Construct 50 kms of access roads (Dyam-Dyam AR – 7 km, Gubevu to Sawutana AR – 4,6 km, Ngxalathi AR – 2 km, Ncerana AR – 2,8 km, Blue Sky AR – 5 km, Ngqwarha to Manyube AR – 3 km, Macibe AR – 7,6 km, Mpahleni AR – 7,1 km, Lusuthu to Masele AR – 3,9 km and Litchi to Qolweni AR – 7 km) by June 2018	0 km
<b>Roads maintenance:</b> 40 kms re-gravelled by June 2018	Regravel 40 km by June 2018	0 km
<b>Revenue enhancement &amp; management:</b> 9 300 indigent beneficiaries subsidised with alternative energy by June 2019	Subsidise 9 300 households with alternative energy by June 2018	0
<b>Transport facilities and operations</b> 1 Taxi rank constructed in Ngqamakhwe by June 2018	Construct one taxi rank in Ngqamakhwe by June 2018	0
<b>Electrification (operation and maintenance plan):</b> Registration of project of street light	Facilitate registration of project on MIS for installation of street lights in Ngqamakwe CBD by June 2018	0



Indicator description	Planned target	Actual Performance
installation along Ngamakwe CBD facilitated by June 2018		
<b>Municipal facilities:</b> One sports field constructed (Kotana - Ward 19) by June 2018	Construct one sport field (Kotana - Ward 19) by June 2018	0
<b>Municipal facilities:</b> One community hall (Mahemini Sokapase) constructed by June 2018	Construct one community hall (Mahemini Sokapase) by June 2018	0
<b>Municipal facilities:</b> Construction of Driver's Licensing and Testing Centre facilitated by June 2018	Facilitate construction of Driver's Licensing and Testing Centre by June 2018	0

### KPA 3: Local economic development

#### Usefulness

#### Measures taken to improve performance not corroborated

#### Various indicators

45. I was unable to obtain sufficient appropriate audit evidence to support the measures taken to improve performance against target as reported in the annual performance report. This was due to limitations placed on the scope of my work. I was unable to confirm the reported measures taken by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported measures taken to improve performance for the indicators listed below:

Indicator description	Planned target	Actual performance
<b>Sustainable rural development:</b> Capacity building of 4 emerging farmers towards implementation of Agri-park projects coordinated by June 2018	Facilitate capacity building of 4 emerging farmers towards implementation of Agri-park projects by June 2018	0
<b>SMMEs:</b> SCM awareness for SMME/cooperatives conducted by June 2018	Conduct SCM awareness to SMMEs/cooperatives by June 2018	0
<b>Programmes management office:</b> Two partnership agreements for Coastal Development (Seagulls) and Bawa Falls coordinated by June 2018	Coordinate two partnership agreements for Coastal development (Seagulls) and Bawa Falls by June 2018	0
<b>SMMEs:</b> Establishment of cooperatives Development Centre coordinated by June 2018	Coordinate establishment of the Cooperatives Development Centre by June 2018	0
<b>Sector plans:</b> Two investment programmes (Revitalisation of Butterworth industries and Gcuwa Dam developments) facilitated by June 2018	Facilitate two investment programmes (Revitalisation of Butterworth industries and Gcuwa Dam developments) by June 2018	0

## Other matters

46. I draw attention to the matters below.

### Achievement of planned targets

47. Refer to the annual performance report on pages ... to ... for information on the achievement of planned targets for the year and explanations provided for the underachievement of a significant number of targets. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information in paragraphs 39 to 47 of this report.

### Adjustment of material misstatements

48. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were in the reported performance information of *KPA2: Basic services and infrastructure development* and *KPA 3: Local economic development*. As management subsequently corrected only some of the misstatements, I raised material findings on the usefulness and reliability of the reported performance information. Those that were not corrected are reported above.

## Report on the audit of compliance with legislation

### Introduction and scope

49. In accordance with the PAA and the general notice issued in terms thereof, I have a responsibility to report material findings on the compliance of the municipality with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.

50. The material findings on compliance with specific matters in key legislations are as follows:

### Annual financial statements and annual report

51. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122(1) of the MFMA. Material misstatements of non-current assets, current assets, liabilities, revenue, expenditure disclosure items identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were provided, but the uncorrected material misstatements and supporting records that could not be provided resulted in the financial statements receiving an adverse audit opinion.

### Strategic and performance management

52. The performance management system and related controls were not maintained or were inadequate as they did not describe how the performance planning, monitoring, measurement, review, reporting and improvement processes should be conducted and organised and managed, as required by municipal planning and performance management regulation 7(1).

## Procurement and contract management

53. Sufficient appropriate audit evidence could not be obtained that all contracts were awarded in accordance with the legislative requirements. Six contractors were paid more than R200 000 but no evidence could be provided of a bidding process followed or approval for deviation. A similar limitation was reported in the prior year.
54. Some of the goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations, in contravention of SCM regulation 17(a) and (c). Similar non-compliance was reported in the prior year.
55. Goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a). Similar non-compliance was reported in the prior year.
56. Some of the contracts were awarded to bidders based on points given for criteria that differed from those stipulated in the original invitation for bidding, in contravention of SCM regulations 21(b) and 28(1)(a) and the Preferential Procurement Regulations. Similar non-compliance was reported in the prior year.
57. Some of the competitive bids were adjudicated by a bid adjudication committee that was not composed in accordance with SCM regulation 29(2). Similar non-compliance was reported in the prior year.
58. Measures to combat the abuse of the SCM system were not implemented as per the requirements of SCM regulation 38(1), because contracts were awarded to providers who had committed a corrupt or fraudulent act in competing for the contract.
59. The preference point system was not applied for the procurement of some goods and services above R30 000, as required by section 2(a) of the Preferential Procurement Policy Framework Act.
60. Some of the contracts were extended or modified without the approval of a properly delegated official, in contravention of SCM regulation 5. Similar non-compliance was reported in the prior year.
61. The performance of some of the contractors or providers was not monitored on a monthly basis, as required by section 116(2)(b) of the MFMA. Similar non-compliance was reported in the prior year.
62. The contract performance and monitoring measures and methods were not sufficient to ensure effective contract management, as required by section 116(2)(c) of the MFMA.
63. Awards were made to providers who were in the service of other state institutions or whose directors or principal shareholders were in the service of other state institutions, in contravention of MFMA 112(j) and SCM regulation 44. Similar awards were identified in the previous year and no effective steps were taken to prevent or combat the abuse of the SCM process, as required by SCM regulation 38(1).
64. Persons in service of the municipality whose close family members had a private or business interest in contracts awarded by the municipality failed to disclose such interest, in contravention of SCM regulation 46(2)(e) or the code of conduct for councillors issued in terms

of the Municipal Systems Act (MSA) or the code of conduct for staff members issued in terms of the MSA. Similar non-compliance was reported in the prior year.

65. Persons in the service of the municipality who had a private or business interest in contracts awarded by the municipality failed to disclose such interest, in contravention of SCM regulation 46(2)(e), the code of conduct for councillors issued in terms of the MSA and the code of conduct for staff members issued in terms of the MSA. Similar non-compliance was reported in the prior year.

### **Consequence management**

66. Unauthorised, irregular and fruitless and wasteful expenditure incurred by the municipality was not investigated to determine whether any person was liable for the expenditure, as required by section 32(2) of the MFMA.

### **Assets management**

67. An adequate management, accounting and information system which accounts for assets was not in place, as required by section 63(2)(a) of the MFMA.
68. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the MFMA.
69. Capital assets were disposed of that were needed to provide the minimum level of basic municipal service, in contravention of section 14(1) of the MFMA.
70. Capital assets were disposed of without the approval of the council, as required by section 14(2)(a) of the MFMA.

### **Revenue management**

71. An adequate management, accounting and information system which accounts for debtors, as required by section 64(2)(e) of the MFMA, was not in place.
72. An effective system of internal control for debtors and revenue, as required by section 64(2)(f) of the MFMA, was not in place.

### **Expenditure management**

73. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
74. Reasonable steps were not taken to prevent irregular expenditure, as required by section 62(1)(d) of the MFMA. The expenditure disclosed does not reflect the full extent of the irregular expenditure incurred and the full extent of the irregular expenditure could not be quantified as indicated in the basis for modified paragraph. Most of the disclosed irregular expenditure was caused by non-compliance with supply chain regulations.
75. Reasonable steps were not taken to prevent fruitless and wasteful expenditure amounting to R4,17 million, as disclosed in note 43 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. Most of the disclosed fruitless and wasteful expenditure was caused by non-compliance with the MFMA.



76. Reasonable steps were not taken to prevent unauthorised expenditure amounting to R276,39 million, as disclosed in note 42 to the annual financial statements, in contravention of section 62(1)(d) of the MFMA. Most of the unauthorised expenditure was caused by non-compliance with the MFMA.

#### **Liability management**

77. An effective system of internal control for liabilities, as required by section 63(2)(c) of the MFMA, was not in place.

#### **Human resources management**

78. Financial interests were not disclosed by the municipal manager and his/her senior managers within 60 days from date of their appointment, as required by regulation 36(1)(a) regarding the appointment and conditions of employment of senior managers.

#### **Other information**

79. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report, which includes the directors' report, the audit committee's report. The other information does not include the financial statements, the auditor's report and those selected objectives presented in the annual performance report that have been specifically reported in this auditor's report.
80. My opinion on the financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and I do not express an audit opinion or any form of assurance conclusion thereon.
81. In connection with my audit, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements and the selected objectives presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
82. I did not receive other information prior to the date of this auditor's report. When I do receive and read this information and if I conclude that it contains a material misstatement, I am required to communicate the matter to those charged with governance and request that the other information be corrected. I may have to retract this auditor's report and reissue and amended report as appropriate. However, if it is corrected this will not be necessary.

## Internal control deficiencies

83. I considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance on it. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for the adverse opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.

- Leadership did not adequately exercise oversight of the general control environment as evidenced by repeat issues raised during the audit. Leadership's tolerance for control deviations was also evident in the application of the municipality's own SCM policy as deviations from this policy were identified. In addition, leadership did not exercise consequence management where there were deviations from internal control requirements.
- The financial disciplines relating to the daily, weekly and monthly processing and reconciliation of transactions were not embedded in the control environment at the municipality. This resulted in misstatements that were identified during the audit.
- Instability during the year under review impacted on the effectiveness of the audit committee and internal audit as planned meetings did not take place. This impacted on the control environment and contributed to the material findings reported in relation to the financial statements, annual performance report and compliance with legislation.

## Other reports

84. I draw attention to the investigation being conducted by the Hawks into allegations of possible fraud and collusion between municipal employees and suppliers in the awarding of contracts. This investigation could have an impact on the matters reported in the municipality's financial statements, reported performance information, compliance with applicable legislation and other related matters. This investigation did not form part of my opinion on the financial statements or my findings on the reported performance information or compliance with legislation. The investigation is still underway and the finalisation date not yet known.

Auditor General

East London

30 November 2018



AUDITOR - GENERAL  
SOUTH AFRICA

*Auditing to build public confidence*

## **Annexure – Auditor-general's responsibility for the audit**

1. As part of an audit in accordance with the ISAs, I exercise professional judgement and maintain professional scepticism throughout my audit of the financial statements, and the procedures performed on reported performance information for selected objectives and on the municipality's compliance with respect to the selected subject matters.

### **Financial statements**

2. In addition to my responsibility for the audit of the financial statements as described in this auditor's report, I also:
  - identify and assess the risks of material misstatement of the financial statements whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations or the override of internal control.
  - obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality's internal control.
  - evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the accounting officer.
  - conclude on the appropriateness of the accounting officer's use of the going concern basis of accounting in the preparation of the financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Mquma Local Municipality's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements about the material uncertainty or, if such disclosures are inadequate, to modify the opinion on the financial statements. My conclusions are based on the information available to me at the date of this auditor's report. However, future events or conditions may cause a municipality to cease operating as a going concern.
  - evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
  - obtain sufficient appropriate audit evidence regarding the financial information of the entity's activities or business activities within the group to express an opinion on the consolidated financial statements. I am responsible for the direction, supervision and performance of the group audit. I remain solely responsible for my audit opinion

### **Communication with those charged with governance**

3. I communicate with the accounting officer regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.
4. I also confirm to the accounting officer that I have complied with relevant ethical requirements regarding independence, and communicate all relationships and other matters that may

reasonably be thought to have a bearing on my independence and, where applicable, related safeguards.